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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1940

No. 78

A. C. FROST & COMPANY,
Petitioner,

vs.

COEUR D'ALENE MINES CORPORATION,
Respondent.

BRIEF FOR RESPONDENT

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Boise, Idaho,
Counsel for Respondent.

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BRIEF FOR RESPONDENT

OPINIONS OF COURTS BELOW

No written opinion was rendered by the trial court, but it adopted findings of fact and conclusions of law. (R. 205-218.) Judgment was rendered July 6, 1938. (R. 218-219.)

The Supreme Court of the State of Idaho filed its final opinion on February 15, 1940 (R. 227-235), which appears in 98 Pac. (2) 965. It has not yet been officially reported.

JURISDICTION

The opinion of the Supreme Court of the State of Idaho held that a contract whereby respondent, the issuing corporation, gave petitioner an option to purchase its stock,

and providing for the sale of such stock to the general public and for the distribution of the proceeds of such sales to them, under which offerings and sales of said stock were in fact made to the public generally, is clearly in violation of the Securities Act of 1933 (Act of May 27, 1933, c. 38, Title 1, 48 Stat. 74, 15 U.S.C.A. 77a et seq.), because the stock was not registered as required thereby; further, the court held that as the contract violated this Federal Statute, it is invalid and unenforceable.

It is the contention of petitioner that jurisdiction is conferred upon this court by the provisions of Sec. 237 (b) of the Judicial Code, as amended.

This court granted a writ of certiorari, October 14, 1940.

STATEMENT OF THE CASE

Petitioner commenced this action in the Idaho State Court to recover damages from respondent for breach of contract. On September 10, 1934, respondent and W. J. Boland entered into a contract which provided that Boland should have the option to purchase from respondent 1,300,000 shares of respondent's stock then in its treasury for 10c a share. Specified monthly payments were required to be made by Boland and stock would be issued to him or his nominee as paid for. A copy of this contract referred to as the "option agreement" is attached to petitioner's complaint and marked Exhibit A (R. 175-178).

It subsequently appeared that Boland was acting as agent for petitioner in obtaining the option agreement, and by instrument dated September 8, 1934, two days before the option agreement, Boland assigned it to petitioner (Plaintiff's Exhibit 8, R. 15).

On April 26, 1935, the option agreement was modified to reduce and alter the required monthly payments which petitioner was required to make. (Finding 5, R. 211.)

On May 15, 1935, this option agreement was again modified as set forth in plaintiff's Exhibit 14 (R. 20). This modification provided for general sales of this treasury stock, and prescribed that ten cents a share out of the purchase price received from such sales was to be credited to petitioner and applied on the payments required under the option agreement. The balance of such purchase price, instead of being paid over to petitioner as formerly, was to be placed in respondent's treasury to be used for the purposes designated in the modification. This money so placed in respondent's treasury was to be paid to petitioner out of the earnings of respondent.

This option contract as modified by these subsequent agreements is the contract upon which petitioner bases its causes of action. (R. 171-172.)

This stock of respondent with which this contract was concerned was not registered with the Securities & Exchange Commission, as required by the provisions of the Securities Act of 1933, or any amendment thereof. (Finding 10, R. 215.) The frequent communications between petitioner and R. W. Nuzum, introduced as Exhibits in this action, show conclusively that petitioner and respondent both realized from the beginning that this stock was not registered under the Securities Act of 1933, and, further, that this Act required such registration in order to make the option agreement and their transactions thereunder lawful.

Petitioner, itself, paid for at ten cents a share, and received under this contract, 165,000 shares of stock. Petitioner and said R. W. Nuzum together sold and disposed of 279,850 shares of this optioned stock to divers other persons, including large blocks of stock sold to and through brokerage houses. (Plaintiff's Ex. 74, R. 95, Defendant's Ex. 94, R. 136; R. 95, 109, 30, 33-37 inc., 67, 68, 69, 74, 76, 86, 115, 116, 122.) These sales were made during the period from

January 31 to August 15, 1935, inclusive. (Plaintiff's Ex. 74, R. 95.) Out of the purchase money received, ten cents a share was placed in the treasury of respondent and credited to petitioner on its option payments. The proceeds over and above this ten cents per share received from these numerous sales to others amounted to $29,306.00. Of this sum, $13,000.00 was paid to petitioner, part of which was paid by petitioner to R. W. Nuzum as a commission, and the balance of $16,306.00 was turned over to respondent and credited to petitioner, to be paid to it out of earnings of respondent, as provided by the modification of May 15, 1935. (Plaintiff's Ex. 74, R. 95.)

During the months of May, June and July, 1935, in addition to the sales above mentioned, petitioner sold 15,000 shares of respondent's stock which it had previously acquired (R. 67), and 140,000 shares which belonged to the Bunker Hill Mine Corporation of Toronto, (R. 67-68), and on which petitioner also had an option to purchase.

During this time the only assets of the respondent corporation were an option to purchase the Mineral Point group of mining claims, on which no payments had been made, and an option to purchase the Lonesome Pine group, on which a small amount had been paid. (R. 54, 66.)

Petitioner paid to respondent under the contract sufficient money and received credit from sales made to others to meet the payments under the option agreement as modified up to and including the payment due October 10, 1935. (Finding 8, R. 213, 214.)

The trial court found (Finding 9, R. 214) that petitioner abandoned all its rights under the contract as modified in the summer of 1935, and thereafter failed to make any of the required payments because of its inability to finance the purchase of the stock; further, that petitioner's failure to perform the contract was not because it was prevented from

so doing by respondent. (Finding 11, R. 215.) On March 13, 1936, respondent notified petitioner of termination of the option agreement. (Finding 11, R. 215.)

Petitioner's first cause of action seeks as damages its anticipated profits from the portion of the contract as modified, which is completely executory on both sides. The trial court denied petitioner any relief on this cause of action. Petitioner's second cause of action is to recover the sum of $16,306.00, which was received by respondent from the sales of the optioned stock to others by petitioner and Nuzum, over and above the ten cents a share, and which was credited to petitioner to be paid out of the earnings of respondent. There is no contention by petitioner that respondent had any earnings out of which this sum could be paid. The trial court allowed recovery on this second cause of action.

Both petitioner and respondent appealed to the Supreme Court of Idaho.

The State Supreme Court held that the option agreement as modified was made in violation of the Securities Act of 1933, and, therefore, was invalid and unenforceable. It sustained the decision of the trial court on the first cause of action, and overruled it on the second, denying petitioner any relief whatsoever. (R. 227-235 inc.)

SUMMARY OF ARGUMENT

The Supreme Court of the State of Idaho held that the contract entered into between respondent and Boland, and by him assigned to petitioner, violated the Securities Act of 1933, and was, therefore, void and unenforceable, and that the parties would be left in the position in which the court found them.

Petitioner, in this appeal, objects to this decision on two grounds:

First, that this is not a transaction involving a public

offering, and is consequently exempt from the provisions of the Act under Sec. 4 (1).

Second, that even though this contract is in violation of the Securities Act, the Idaho Court should not have refused to enforce it.

These two questions will hereafter be discussed in that order.

It is conceded in this action that the stock involved is a "security" as defined by the Securities Act, Sec. 2 (1); that these securities were sent through the mail and transferred in interstate commerce, and that the contract itself, the assignment, and all modifications of the contract, were entered into through use of the mails and interstate commerce (R. 53); and that these securities were not registered with the Securities & Exchange Commission. Further, that respondent is an issuer as defined by Sec. 2 (4) of the Act.

It appears from the evidence that, so far as petitioner is concerned, most of the transactions and correspondence were carried on by A. C. Frost, petitioner's President, but they were all for and on behalf of petitioner itself. (R. 52.)

Petitioner in its brief (p. 9) refers to the opinion of the Supreme Court of Idaho before it was modified after the petition for rehearing was filed. But this Court will only consider the final opinion of the State Supreme Court, and will not consider any temporary or intermediate opinion before it is filed in its final form. Grayson v. Harris, 267 U.S. 352, 69 L. ed. 652 (1924).

This court will not disregard the explicit holding of the State Court as to the basis of its decision. Guaranty Trust Co. v. Blodgett, 287 U.S. 509, 77 L. ed. 463 (1932).

ARGUMENT

I

As this transaction involves a public offering there is no

exemption from the operation of the Securities Act of 1933.

Petitioner asserts that this option agreement as modified is exempt from the requirements of the Securities Act of 1933, because it is not a transaction "involving any public offering", as provided in Sec. 4 (1) of the Act, and, therefore, it was not necessary for the stock of respondent to be registered as required by the Act.

The State trial court held that this contract (where this "agreement" or "contract" is mentioned herein, it refers to the original option agreement as modified, which forms the sole basis for petitioner's action), was entered into in violation of the provisions of the Act, and refused to accept the contention of petitioner that no public offering was involved. (Finding 10, R. 215.)

The Supreme Court of Idaho carefully considered the record and exhibits in this case, and ruled that the Securities Act was violated by the parties by entering into this agreement and by their operations under it, and that it clearly appeared that no exemption could be claimed on the ground there was no public offering. (98 Pac. (2) 965.) The court said at page 967:

> "The proof rather than sustaining the burden of showing that the transaction was exempted affirmatively shows that all the stock offered for sale amounted to public offerings and that interstate means of communication and transportation were used in connection therewith. Certainly the facts disclosed by the option agreement itself and the so-called subsequent modification by letters, etc., and the many letters passing between Frost & Company and Coeur d'Alene Mines Company, recognizing that Frost & Company was selling the treasury stock to all and sundry, directing delivery of such treasury stock to other stock firms or brokers for sale to or by them flatly refutes such contention as does likewise the case of Securities & Exchange Commission v. Sunbeam Gold Mining Co., 9 Cir., 95 F. (2) 699."

No claim is made by petitioner that the Securities Act does not apply to this transaction and require the registration of the stock, except the one ground that it is exempt by the provisions of Sec. 4 (1) of the Act. As petitioner is claiming relief from the operation of the Act under an exemption, the burden is on petitioner to prove that the transaction comes within the terms of the exemption; furthermore, the terms of an exception are strictly construed against a claimant of its benefit.

Spokane & I. E. R. Co. vs. United States, 241 U.S. 344, 60 L. ed. 1037 (1915);

Securities & Exchange Commission v. Sunbeam Gold Mines Co., 95 Fed. (2) 699 (1938).

As was held by both the State courts, not only does the evidence disclose that petitioner has failed to maintain its burden of showing that there was no public offering, but rather it conclusively appears that the transaction involved a public offering of these securities.

The original option was modified by agreement of the parties, and the terms of this modification are set forth in plaintiff's Ex. 14. It is this altered contract which forms the basis for both of petitioner's causes of action. This contract not only provides that petitioner has an option to purchase the treasury stock of respondent at ten cents a share, but also that there shall be a general sale of this stock so optioned; that ten cents a share of the purchase price received from such sales shall be credited to petitioner on its option payments; that the balance of the proceeds shall be turned over to respondent for specified purposes, and that the amount of these sums shall be paid to petitioner out of the earnings of respondent.

The agreement of September 10, 1934, specifically provided that the stock should be issued to Boland *or his*

nominee (plaintiff's Ex. 9, R. 14), thus showing that sales of the stock by Boland was contemplated. Consequently, by the very terms of the agreement itself it was provided for general sales of the stock by the parties. That this conclusion is correct unavoidably appears from an examination of the acts of the parties under and pursuant to the contract.

As early as the end of January, 1935, 20,000 shares of stock were sold to or by Starmount. (Plaintiff's Ex. 25, R. 28; Plaintiff's Ex. 26, R. 29; Plaintiff's Ex. 27, R. 30.)

By the first of February, 1935, petitioner realized that it was necessary to comply with the Securities Act, and thereafter frequently urged compliance therewith. (Exs. 33, 34, 35, 36, 37, 38, 39, 40, 68, 41, 48, 17, 42.) This conclusion was reached after taking the matter up with an attorney (plaintiff's Ex. 37, 40). So it appears that there was never any doubt in the mind of petitioner but that this contract and the sales which were being made under it by petitioner and Nuzum were within the provisions of the Securities Act, and that registration of this stock was required. Indeed, so anxious was petitioner to have this stock registered that it intimated that it might be advisable not to disclose the existence of the option. (Defendant's Exs. 48, 65.)

A. C. Frost, petitioner's President, wrote Nuzum on February 1, 1935, that it was important that the stock be listed on some exchange—"but whichever offers the best advantage for trading purposes". (Plaintiff's Ex. 33, R. 42.) Obviously, petitioner was interested in trading in this stock, and not in holding it as an investment.

The following day, February 2, 1935, Frost again wrote Nuzum concerning the listing of the stock, and said, "If in the application the Company admits that the stock is assessable it will certainly detract from the value of the stock and the marketing of it". (Plaintiff's Ex. 34, R. 43.) Again, it

appears that trading in the stock was petitioner's chief interest.

In plaintiff's Exhibit 35 (R. 43), a letter from Frost to Nuzum, he again speaks about establishing a market for the stock.

The letter from Frost to Nuzum, dated February 6, 1935, (defendant's Ex. 67, R. 90), contemplates the sale of a large block of stock to Gibson & Co., and a sale of 80,000 shares to this concern was made on May 8, 1935. (R. 30, 69, 76, 115, 122.) Petitioner actually consummated this sale itself. (R. 30, 74, 86.)

Plaintiff's Exhibit 37 (R. 44), a letter from A. C. Frost to R. W. Nuzum, dated February 15, 1935, disclosed that petitioner's object under the contract was to market the stock, and not hold it for investment.

Again, by letter dated February 16, 1935, Frost exhibits his impatience concerning the listing of the stock. Also he appears to be pleased about a favorable article appearing in a newspaper. (Plaintiff's Ex. 38, R. 45.) Frost remarks that it will take two or three months to get the stock listed, and then says, "and it will probably consume most of the time we have in which to meet the first $25,000.00 payment on the purchase price of the Mineral Point property". When it is remembered that this option covered almost all of the stock in respondent's treasury (Finding 3, R. 209; R. 110), if this contract were merely a sale by respondent to a single person for an investment, neither petitioner nor respondent would have any interest in listing the stock on an exchange and marketing it. This letter discloses that the stock was to be marketed to raise funds to make respondent's payment under the option on mining claims. The contract was merely a device to accomplish general sales of the stock to the public.

On April 23, 1935, petitioner wrote respondent as follows:

"By reason of *present* market conditions, you may

deal with the treasury stock as you see fit." (Emphasis ours.) (Defendant's Ex. 50, R. 65.)

At the time of trial Frost stated that this letter did not mean what it said and that it was given to facilitate registering the stock with the Securities & Exchange Commission. (R. 65, 86-88 inc.) However, it does show that market conditions were of utmost importance at this time. Nuzum testified that the letter was written because Frost was having difficulty selling the stock. (R. 146.)

Frost wrote a letter to Nuzum dated May 6, 1935, approving the sale of 10,000 shares of this stock. (Defendant's Ex. 66, R. 82.)

On May 11, 1935, petitioner agreed to pay R. W. Nuzum a share of the profits resulting from sales to others, both past and future. (Defendant's Ex. 55, R. 76.) The letter recites that this was in accordance with a proposition made by petitioner "some months ago".

On May 20, 1935, a special meeting of the Board of Directors of petitioner was held and the modification of the contract as set forth in plaintiff's Exhibit 14 was approved, with the following language:

"After a full discussion, the said letter recited in said Resolution was confirmed on the condition and with the understanding that the remaining one million (1,000,000) shares of treasury stock, covered by the option agreement of September 10, 1934, *can be taken up and paid for as and when it is most advantageous to market same* * * *" (Emphasis ours.) (Plaintiff's Ex. 16, R. 22.)

Petitioner was very concerned over the engineers' reports on the mining property, not it appears because he was interested in its values, but because of possible adverse effect on market conditions. (Plaintiff's Exs. 35, 17, 42.)

Plaintiff's Exhibits 28, 29, 43 and 30 disclose the agree-

ment to sell 20,000 shares of the stock to the J. E. Jones Brokerage Corporation. This sale was agreed to by petitioner. (R. 33-37 inc., 69, 86, 116.) Ten cents a share from the purchase price was credited on the option payments, and the balance was given to petitioner, who paid Nuzum a 25 per cent. commission. (R. 33-37 inc.)

Defendant's Exhibit 63 (R. 82) shows that it was contemplated to sell a large block of this stock before it was listed with the Securities & Exchange Commission, to provide funds for respondent to make the payment on the option to purchase the Mineral Point claims.

On July 8, 1935, petitioner sent to Nuzum a certificate representing 5,000 shares of this stock, and requested him to sell it. Petitioner also stated that it desired to sell 25,000 or 30,000 additional shares during that week. (Defendant's Ex. 70, R. 91.) Nuzum replied that it was impossible to sell the stock at that time, and gave as one of the reasons that the stock which petitioner had sold to Gibson & Co. had flooded the market. (Defendant's Ex. 71, R. 92.)

A. C. Frost testified at the trial of this cause that one method of taking up the optioned stock which was followed was to market the stock generally. "The stock was delivered to the prospective—or the purchaser, and credited to our option contract". (R. 27.)

Again, Frost testified that sales of the stock and attempts to sell the stock were "discontinued" after June 29, 1935 (R. 50), thus showing that sales and offerings had been made prior to that time.

D. E. Watson, Secretary of respondent, in identifying plaintiff's Exhibit 74 (R. 95), stated, "Well, it is an account of stock that was sold during the spring of 1935 by R. W. Nuzum and A. C. Frost * * *" (R. 95.) Petitioner's witness E. C. Daniels also testified that a large number of sales were made during this period. (R. 118.)

The evidence pertinent to the question of whether this transaction involved a public offering of this stock has been outlined in considerable detail in order that a comprehensive picture might be presented to the court. The contract as modified by its very terms provides for sales of this stock to the public generally, and for the distribution of the proceeds of such sales. The evidence conclusively shows that both parties contemplated throughout that sales of stock to the public would be offered and made from time to time, and the condition of the market price of this stock was always uppermost in petitioner's mind. Respondent's chief asset was an option to purchase the Mineral Point claims; no payment had been made under this option, and the date of the first payment was approaching. Funds to meet this payment were to be raised by the marketing of the stock by petitioner and Nuzum. This in itself shows that this was no ordinary contract for the sale of stock to a single individual, for if it were, respondent would not benefit by the sale of stock by petitioner, and petitioner would not be anxious to sell the stock to secure funds with which respondent would make its payment.

During the whole time petitioner paid for and received only 165,000 shares of this stock. Yet it and Nuzum sold to the public generally 279,850 shares, and, in addition, petitioner at the same time sold 15,000 shares which it had previously acquired and 140,000 shares belonging to the Bunker Hill Mines Corporation of Toronto, which it had under option. In the face of such an active sales effort on the part of petitioner, it is difficult to understand petitioner's contention that only a single sale of stock to petitioner was involved, that it was purchasing for an investment, and that there was no public offering of the stock.

Petitioner not only actively assisted in the sale to many persons of the 279,850 shares, but received credit of ten

cents a share on its option payments. The balance of the proceeds over and above this ten cents a share amounted to $29,306.00. Petitioner received $13,000.00 of this sum in cash, and the balance was credited to its account to be paid to it out of the earnings of respondent.

Not only has petitioner failed to maintain the burden of establishing that this transaction did not involve a public offering and thus bring it within the exemption of Sec. 4 (1) of the Securities Act, but it conclusively appears that a public offering was specifically provided for by the contract, contemplated throughout by the parties, and effectively consummated in fact. Both the State trial court and the Supreme Court of Idaho so held.

II

A contract made in violation of the Securities Act is void and unenforceable.

The Supreme Court of Idaho held (98 Pac. (2) 965), that as this contract violated the provisions of Sec. 5 of the Securities Act, it is void and unenforceable.

Sec. 5 provides that it is "unlawful" to use the mails or any means or instruments of transportation or communication in interstate commerce to sell or offer to buy an unregistered security, or to deliver the security. Thus, Congress has not only required the registration of securities, but in addition has declared that a violation of the Act is "unlawful".

The Idaho Court in rendering its decision followed the general and well established rule of law that a contract made in violation of statute is void, and the courts are not open to either party to an illegal contract to enforce its wrongful objects.

This court said in Bank of U.S. v. Owens, 2 Pet. 527, 7 L. ed. 508 (1829), in holding unenforceable a contract made in violation of law:

"The answer would seem to be plain and obvious, that no court of justice can in its nature be made the handmaid of iniquity. Courts are instituted to carry into effect the laws of a country; how can they then become auxiliary to the consumation of violations of law?"

"There can be no civil right where there can be no legal remedy; and there can be no legal remedy for that which is itself illegal."

This general rule of law has been long and widely applied; and there is no exception where the statute does not specifically declare such contracts void, as appears from the following cases:

Anderson v. Carkins, 135 U.S. 483, 34 L. ed. 272 (1889);

Weil v. Neary, 278 U.S. 160, 73 L. ed. 243 (1928);

Awotin v. Atlas Exchange National Bank, 295 U.S. 209, 79 L. ed. 1393 (1934);

Hannay v. Eve, 3 Cr. 242, 2 L. ed. 427 (1806);

Louisville & N. Ry. Co. v. Mottley, 219 U.S. 467, 55 L. ed. 297 (1910);

Smith v. McCullough, 270, U. S. 456, 70 L. ed. 682 (1925);

Texas & Pac. Ry. Co. v. Pottorff, 291, U. S. 245, 78 L. ed. 777 (1933);

Craig v. Missouri, 4 Pet. 410, 7 L. ed. 903 (1830);

Hall v. Coppell, 7 Wall, 542, 19 L. ed. 244 (1868);

Lingle v. Snyder, 160 Fed. 627 (1908);

McFall v. Arkoosh, 37 Ida. 243, 215 Pac. 978 (1923);

Pacific Elec. Ry. Co. v. Bond & Cas. Ins. Co., 55 Cal. App. 704, 204 Pac. 262 (1921);

Crawford v. McConnell, 173 Okla. 520, 49 Pac. (2) 551 (1935);

Williston on Contracts, Vol. 6, Sec. 1764, n. 70.

The same rule has been applied, and courts have refused

to enforce a contract made in violation of law where the same phraseology is used as is found in the Securities Act, i. e., that certain acts are declared to be "unlawful".

Glass v. Basin & Bay State Mining Co., 31 Mont. 21, 77 Pac. 302 (1904);

Holm v. Bramwell, 20 Cal. App. (2) 332, 67 Pac. (2) 114 (1937).

In addition to prohibiting the acts and transactions prescribed therein, the Securities Act also provides in Sec. 24 that a wilful violation of any of the provisions of the Act is a criminal offense and shall be punished by a fine of not more than $5,000.00, or imprisonment for not more than five years, or both.

A contract made in violation of a criminal statute, or a transaction in furtherance of a criminal enterprise is void and the courts will not give their aid to assist any party thereto. It will leave the parties where it finds them.

Davidson v. Lanier, 4 Wall. 447, 18 L. ed. 377 (1866);

Libby v. Pelham, 30 Ida. 614, 166 Pac. 575 (1917);

Short v. Bullion-Beck & C. Min. Co., 20 Utah, 20, 57 Pac. 720 (1899);

Delgado v. Delgado, 42 N. Mex. 582, 82 Pac. (2) 909 (1938);

Asher v. Johnson, 26 Cal. App. (2) 403, 79 Pac. (2) 457 (1938).

An exception to this general rule of law exists when it affirmatively appears from the language of the statute itself, from the purpose of the act, and from the evil that it is meant to correct, that it was the clear intention of the lawmaking body that a contract made in violation of the statute should, nevertheless, be valid and enforceable.

Cf. Dunlop v. Mercer, 156 Fed. 545 (1907).

It should be emphasized that this is an exception to the general rule. It is not necessary for the court to find that the Legislature intended that all contracts violating a statute are void before so holding. On the contrary, the court shall declare such contracts invalid and unenforceable, unless it shall be satisfied that the Legislature had a clear affirmative intent that such agreements should be valid.

A party claiming under an exception to a general rule of law has the burden of establishing that he clearly comes within such exception.

Spokane & I. E. Ry. Co. v. United States, supra;
Securities & Exchange Commission v. Sunbeam Gold Mines Co., supra.

An examination of the Securities Act as a whole discloses that it was never the intent of Congress that it should fall within the above expressed exception. Rather, it obviously appears that, unless contracts made in violation of the Act and to further enterprises declared unlawful by it are void, the objects of the Act will be defeated.

The purpose of the Act is to protect the public from the sale of worthless securities and from fraudulent and deceitful selling methods. Consequently, registration of the security and approval of the prospectus is required. The chief aim is to protect the purchaser and, therefore, certain specific civil remedies are given a purchaser against a seller who does not comply with the requirements of the statute (Sec. 12). But these remedies are efficacious and the purchaser receives redress only if the seller is financially responsible. In the ordinary case of an issuing corporation, if it is successful the buyer of its securities is not injured and does not complain. It is when such corporation fails that the buyer is harmed, and then of course his only remedy is to exchange his worthless stock for an empty lawsuit without hope of

actual recovery. The same result applies to financially irresponsible underwriters and dealers. Therefore, the maximum protection can be given to the investing public, the only object of the Act, only by declaring void contracts which violate the Act, and by the refusal of the courts to give their aid and sanction to unlawful transactions which disregard the mandatory requirements established by Congress.

McManus v. Fulton, 85 Mont. 170, 278 Pac. 126, 67 A.L.R. 690 (1929);

Brandenburg v. Miley Petroleum Exploration Co., 16 Fed. (2) 933 (1926);

See note 87 A.L.R. 42, at page 98.

Take, for example, the case at bar. Petitioner was obviously in serious financial straits, and respondent had no assets except a couple of options on mining property on which no payments had been made; it was having great difficulty meeting its monthly payroll. To whom could all the purchasers of the 279,850 shares of stock sold by petitioner and respondent look for reimbursement? If contracts such as this one are upheld and approved by the courts, the Securities Act is, for such purchasers, an empty gesture. Then, an issuer can without fear of loss disregard the requirements of registration, make contracts with others to accomplish the sale of its stock to the public generally, and even go so far as to employ deceit and fraud. If the enterprise of the issuer is successful, the purchasers will not object, and, if it is unsuccessful and its assets dissipated, it has nothing it can lose nor that can be recovered by its disgruntled stockholders.

The only certain method of providing adequate protection for the buying public is to check such wilful violations of the Act at their inception. The purpose of the Act is to prevent unregistered securities from being offered to the

public; not merely to give the purchasers an opportunity to recover their losses through the courts — too often a remedy in name only. Such protection can be afforded only by the courts refusing to approve and uphold contracts which violate the statute, particularly when, as in the case at bar, they are obviously designed to, and actually do, accomplish offerings and sales of unregistered issues to the general public. Judicial approval of these unlawful contracts will encourage issuers to disregard the Act, and their failure to comply with its requirements can only result in injury to the public which this Act was designed to protect.

It is urged by petitioner in its brief (p. 17, 19) that registration of securities under the Securities Act is purely voluntary; that Congress did not intend to prohibit the sale in interstate commerce of unregistered securities. However, it should be noticed that Congress incorporated a criminal provision into the law, carrying a harsh penalty. It would be equally absurd to assert that criminal statutes for fraud, larceny, arson, or any other crime do not intend to prohibit such illegal acts—it is merely that if someone violates them they subject themselves to the penalty.

Although petitioner makes no denial of it in its brief, it should be pointed out that both the parties to the contract were in pari delicto. A brief examination of the mass of correspondence, hereinbefore referred to, shows that petitioner realized from the inception that these securities were required to be registered by the Securities Act and that they were not so registered. (See also R. 82-83).

The first cause of action as set forth in petitioner's complaint seeks recovery as damages of its anticipated profits based on that portion of the contract which is wholly unexecuted by either party, and bases its estimate of the damages on the current market price of the stock in June, 1935. Petitioner has neither given up anything nor changed its posi-

tion to its disadvantage in reliance on this illegal contract.

By its second cause of action petitioner is attempting to recover profits from sales of this unregistered stock which it and Nuzum made to the general public. And still petitioner maintains (brief, p. 26) that the Idaho Supreme Court erred in holding that it was selling this stock to the public.

Both of these causes of action are based squarely upon the contract, and petitioner has never asserted otherwise. The contract violates the provisions of the Securities Act of 1933, and is, therefore, void and unenforceable.

CONCLUSION

The judgment of the Supreme Court of Idaho should be affirmed.

Respectfully submitted,

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APPENDIX

Pertinent provisions of the Securities Act of 1933, c. 38, Title I, 48 Stat. 74, 77, 87 (15 U.S.C.A. 77a et seq.):

Sec. 2 (15 U.S.C.A. 77b):

"When used in this subchapter, unless the context otherwise requires—

(1) The term 'security' means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, pre-organization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, or, in general, any interest or instrument commonly known as a 'security', or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing."

* * *

"(4) The term 'issuer' means every person who issues or proposes to issue any security; except that with respect to certificates of deposit, voting-trust certificates, or collateral-trust certificates, or with respect to certificates of interest or shares in an unincorporated investment trust not having a board of directors (or persons performing similar functions) or of the fixed, restricted management, or unit type, the term 'issuer' means the person or persons performing the acts and assuming the duties of depositor or manager pursuant to the provisions of the trust or other agreement or instrument under which such securities are issued; except that in the case of an unincorporated association which provides by its articles for limited liability of any or all of its members, or in the case of a trust, committee, or other legal

entity, the trustees or members thereof shall not be individually liable as issuers of any security issued by the association, trust, committee, or other legal entity; except that with respect to equipment-trust certificates or like securities, the term 'issuer' means the person by whom the equipment or property is or is to be used; and except that with respect to fractional undivided interests in oil, gas, or other mineral rights, the term 'issuer' means the owner of any such right or of any interest in such right (whether whole or fractional) who creates fractional interests therein for the purpose of public offering."

Sec. 4 (15 U.S.C.A. 77d):

"The provision of section 77e (Sec. 5) shall not apply to any of the following transactions:

(1) Transactions by any person other than an issuer, underwriter, or dealer; transactions by an issuer not involving any public offering; or transactions by a dealer (including an underwriter no longer acting as an underwriter in respect of the security involving in such transaction), except transactions within one year after the first date upon which the security was bona fide offered to the public by the issuer or by or through an underwriter (excluding in the computation of such year any time during which a stop order issued under section 77h is in effect as to the security), and except transactions as to securities constituting the whole or a part of an unsold allotment to or subscription by such dealer as a participant in the distribution of such securities by the issuer or by or through an underwriter."

Sec. 5 (15 U.S.C.A. 77e):

"(a) Unless a registration statement is in effect as to a security, it shall be unlawful for any person, directly or indirectly—

(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell or offer to buy such security through the use or medium of any prospectus or otherwise; or

(2) to carry or cause to be carried through the mails or in interstate commerce, by any means or instruments of transportation, any such security for the purpose of sale or for delivery after sale.

(b) It shall be unlawful for any person, directly or indirectly—

(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to carry or transmit any prospectus relating to any security registered under this subchapter, unless such prospectus meets the requirements of section 77j; or

(2) to carry or to cause to be carried through the mails or in interstate commerce any such security for the purpose of sale or for delivery after sale, unless accompanied or preceded by a prospectus that meets the requirements of section 77j."

Sec. 12 (15 U.S.A. 771): Any person who—

(1) sells a security in violation of section 5; or

(2) sells a security (whether or not exempted by the provisions of section 3, other than paragraph (2) of subsection (a) thereof), by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of

reasonable care could not have known, of such untruth or omission,

shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security.

Sec. 24 (15 U.S.C.A. 77x):

"Any person who willfully violates any of the provisions of this subchapter, or the rules and regulations promulgated by the Commission under authority thereof, or any person who willfully, in a registration statement filed under this subchapter, makes any untrue statement or a material fact or omits to state any material fact required to be stated therein or necessary to make the statements therein not misleading, shall upon conviction be fined not more than $5,000 or imprisoned not more than five years, or both."

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